
United States Circuit Court of Appeals
FOR THE NINTH CIRCUIT

No. 10962

THE RAILROAD CREDIT CORPORATION, a Corporation,
Appellant,
vs.

FREDERICK H. ECKER, FRANK C. WRIGHT and ROBERT E.
COULSON, the members of the Reorganization Committee of the
Western Pacific Railroad Company, Debtor,
Appellees,
and

THE WESTERN PACIFIC RAILROAD CORPORATION,
a Corporation,
Appellant,
vs.

THE RAILROAD CREDIT CORPORATION, a Corporation,
Appellee.

BRIEF ON BEHALF OF APPELLEES FREDERICK H.
ECKER, FRANK C. WRIGHT, AND ROBERT E. COUL-
SON, THE MEMBERS OF THE REORGANIZATION
COMMITTEE OF THE WESTERN PACIFIC RAILROAD
COMPANY, DEBTOR

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SON, THE MEMBERS OF THE REORGANIZATION COM-
MITTEE OF THE WESTERN PACIFIC RAILROAD
COMPANY, DEBTOR**

Statement of the Case

On September 14, 1944, the District Court of the United States, Northern District of California, Southern Division, made an order construing the plan of reorganization of The Western Pacific Railroad Company and reconciling inconsistencies therein (TR-10962, p. 143). This appeal by The Railroad Credit Corporation is from paragraph (3) of that order, which provides (TR-10962, p. 147):

“(3) That the provisions of subdivisions P and R
of the plan of reorganization, which relate to the ap-

plication of the proceeds of the distributive shares of the debtor and its subsidiaries under the marshaling and distributing plan of 1931, be and are hereby construed as requiring a reduction in the number of shares of common stock allocated to The Railroad Credit Corporation under paragraph 4 of subdivision P of the plan by one share for each \$62 of such proceeds received by the Railroad Credit Corporation after December 31, 1938, and prior to the issuance of the new securities under the plan;”

During the period stated in paragraph (3) of the District Court’s order, The Railroad Credit Corporation received proceeds of the distributive shares of the debtor and its subsidiary in the aggregate amount of \$27,094* and applied this sum in reduction of interest upon its claim. Accordingly, upon the issuance of the new securities under the plan of reorganization, the number of shares of common stock of the debtor allocated to the Credit Corporation was reduced by 437 shares.

By this appeal The Railroad Credit Corporation seeks a reversal of paragraph (3) of the District Court’s order and the issuance to the Credit Corporation of 437 shares of common stock of the reorganized Western Pacific Railroad Company.

Proceedings Prior to District Court’s Construction Order

The reorganization proceeding of The Western Pacific Railroad Company was before this Court in 1941 in No. 9714. The history of that proceeding is stated briefly in the Transcript of Record in No. 9714, at pages 1019 and following. Reference is made to the following matters which are pertinent upon this appeal.

* At the time of the hearing upon the Reorganization Committee’s petition for construction (June 2, 1944), the aggregate amount received by The Railroad Credit Corporation was \$26,091.72 (TR-10962, p. 129). This total was increased to \$27,094 by a distribution in December, 1944.

On August 2, 1935, The Western Pacific Railroad Company filed its petition for reorganization under Section 77 of the Bankruptcy Act (47 Stat. 147, c. 204, as amended; 11 U. S. C., § 205) in the District Court of the United States for the Northern District of California, Southern Division. A copy of the petition was filed with the Interstate Commerce Commission. On the same date, the Court entered an order approving the petition as properly filed, providing for the operation of the railroad subject to the supervision and control of the Court, and restraining and enjoining all persons and corporations holding collateral theretofore pledged by the debtor as security for its notes and obligations, from selling, converting or otherwise disposing of such collateral or any part thereof until further order of the Court (TR-9714, p. 18, par. 9). This restraining order and injunction has not been modified or revoked (TR-9714, p. 1020, par. 4).

Subsequently claims were duly filed by or on behalf of various bondholders and creditors (including the claim of The Railroad Credit Corporation) and by the sole stockholder of the debtor Company.

A number of plans of reorganization and modified plans were filed with the District Court and the Interstate Commerce Commission in 1936, 1937 and 1938, and, after proceedings and hearings pursuant to Section 77 of the Bankruptcy Act, the Interstate Commerce Commission, on October 10, 1938, issued its Report and Order approving a plan of reorganization formulated by the Commission (TR-9714, pp. 194, 281). Various parties to the proceeding before the Commission filed petitions for rehearing and modification of the Commission's Report and Order and the plan of reorganization approved therein, and, after rehearing, the Commission, on June 21, 1939, issued its Report and Order on further consideration, approving a modified plan of reorganization, modifying the Report of October 10, 1938, and revoking the Order of October 10, 1938 (TR-9714, pp. 300, 362). No further modification of this plan was made

by the Commission, and, on September 28, 1939, the Commission certified this plan to the District Court. Hearings and arguments were had before the District Court in December, 1939, and January, 1940, and, on August 15, 1940, the Court rendered its opinion and entered an order approving in all respects the plan of reorganization certified by the Commission (TR-9714, pp. 1569, 1600).

Upon appeals from the District Court's order of approval, this Court, on November 28, 1941, reversed the order of the District Court which approved the plan (*In re Western Pac. R. Co.*, 124 F. 2d 136). The Supreme Court of the United States granted certiorari to review the order of this Court, and, on March 15, 1943, reversed the order of this Court and affirmed the order of the District Court approving the plan in all respects (*Ecker v. Western Pacific R. Corp.*, 318 U. S. 448, 63 Sup. Ct. 692).

The plan was then submitted by the Commission to the several classes of secured creditors for acceptance or rejection and was accepted by The Railroad Credit Corporation and all other classes.

The appellees, Frederick H. Ecker, Frank C. Wright, and Robert E. Coulson, were designated as members of the Reorganization Committee to carry out the plan of reorganization pursuant to subdivision R of the plan, and were approved by the District Court by its order entered October 11, 1943. As members of the Reorganization Committee, the appellees were charged with the duty of making provision for carrying out the plan of reorganization under the supervision of the District Court (subd. R of the plan, TR-9714, pp. 395-6).

In the performance of their duties as members of the Reorganization Committee, appellees filed with the District Court on May 9, 1944, a petition for an order construing the plan of reorganization in various respects and reconciling inconsistencies therein (TR-10962, p. 69). This petition

brought before the District Court for determination four questions. The first related to the allotment of common stock to first mortgage bondholders under the provisions of the plan, and the fourth related to the construction of certain provisions in the plan for the determination of available net income for each calendar year, matters which are not in issue upon this appeal. The second related to the retention by The Railroad Credit Corporation of proceeds from the distributive shares of the debtor and its subsidiaries under the Marshalling and Distributing Plan of 1931, and the provisions of the plan for a consequent reduction in the Credit Corporation's claim against the debtor Company and in the amount of securities to be issued to the Credit Corporation in the reorganization. The third related to the disposition of the accommodation collateral pledged with The Railroad Credit Corporation by The Western Pacific Railroad Corporation.

On September 14, 1944, the District Court made its order construing the plan of reorganization, and reconciling inconsistencies therein, pursuant to the opinion of the Court dated June 21, 1944 (TR-10962, pp. 98, 143). The Railroad Credit Corporation has appealed from paragraph (3) of the District Court's order (quoted on pages 1 and 2 of this brief) and from the supporting finding and conclusion of the District Court contained in paragraph (b) of the findings and conclusions (TR-10962, p. 149). The Western Pacific Railroad Corporation has appealed as against The Railroad Credit Corporation from paragraph (5) of the District Court's order (TR-10962, p. 150). No appeal has been taken from any other provision of the order.

The Reorganization Committee is interested only in the appeal of The Railroad Credit Corporation from paragraph (3) of the order and the supporting finding thereto. Acting under its duty to carry out the provisions of the plan of reorganization, the Reorganization Committee took the position that the provisions of subdivisions P and R of the plan, relative to the retention by The Railroad Credit Corporation

of the distributive shares of the debtor and its subsidiaries under the Marshalling and Distributing Plan of 1931, required a reduction in the number of shares of common stock to be issued to The Railroad Credit Corporation upon consummation of the reorganization, and the District Court sustained the position taken by the Reorganization Committee.

While the Reorganization Committee in its petition asked the District Court to determine the status of the third party collateral held by The Railroad Credit Corporation, since that collateral consisted of claims against subsidiaries of the debtor Company and might be deemed to affect the consummation of the reorganization and the securities distributable upon such consummation, the Committee did not take any position or make any recommendation to the District Court in respect of the controversy between The Railroad Credit Corporation and The Western Pacific Railroad Corporation. The Committee, therefore, has no interest upon this appeal in sustaining or questioning paragraph (5) of the District Court's order, from which The Western Pacific Railroad Corporation has appealed.

The Issue Before This Court

The Committee takes the position that the appeal of The Railroad Credit Corporation from paragraph (3) of the District Court's order presents one single issue and only one issue—namely, the question of construction of certain provisions of the plan of reorganization. The issues presented by the appeal of The Western Pacific Railroad Corporation from paragraph (5) of the District Court's order are entirely distinct, do not involve the construction of any provisions of the plan and relate to matters which are no concern of the Reorganization Committee. The consolidation of the two appeals before this Court is purely fortuitous. They involve different parties and raise different issues.

The appellees, Frederick H. Ecker, Frank C. Wright, and Robert E. Coulson, as members of the Reorganization

Committee, will deal in this brief only with the question of construction of the provisions of subdivisions P and R of the plan of reorganization presented by the appeal of The Railroad Credit Corporation from paragraph (3) of the District Court's order. The voluminous brief submitted on behalf of The Railroad Credit Corporation, as appellant, states at considerable length the history of the reorganization proceedings and the provisions of the plan of reorganization, and contains an extended argument as to the merits of certain provisions of the plan, the full priority doctrine of *Northern Pacific Ry. Co. v. Boyd*, 228 U. S. 482, 33 Sup. Ct. 554, and other matters of bankruptcy law. The Reorganization Committee believes that these matters discussed in the brief on behalf of the Credit Corporation, and the larger part of the argument therein contained, are entirely beside the point.

Stated briefly and simply, the issue is this: The plan of reorganization of the Railroad Company, as formulated and approved by the Interstate Commerce Commission, was approved in all respects by the District Court, the action of the District Court was affirmed by the Supreme Court of the United States, and, following a favorable vote upon the plan by all classes of secured creditors including the Credit Corporation, the plan was finally confirmed by the District Court on October 11, 1943. Under these circumstances, the fairness of the plan to the Credit Corporation and its conformity to the full priority doctrine of the *Boyd* case are no longer open to question. The District Court was asked by the Reorganization Committee to construe the provisions of the plan relating to the marshalling and distributing payments retained by the Credit Corporation, and the Court made its determination. In consequence, the only question before this Court is whether the determination of the District Court contained in paragraph (3) of its order of September 14, 1944, is supported by the provisions of the plan. There is a further question whether that determination is open to review upon this appeal.

POINT I

The decision of the District Court that the provisions of subdivisions P and R of the Plan of Reorganization, which relate to the application of the proceeds of the distributive shares of the debtor and its subsidiaries under the Marshalling and Distributing Plan of 1931, require a reduction in the securities allocated to The Railroad Credit Corporation under the Plan, is in accordance with and supported by the express provisions of the Plan of Reorganization.

1. The Provisions of the Plan

For the convenience of the Court, we will here set forth the applicable provisions of the plan which were presented to the District Court for construction, together with extracts from the reports of the Commission which shed light upon their meaning.

Paragraph 4 of subdivision P of the plan provides:

“4. The Railroad Credit Corporation shall receive in respect of its claim in the principal amount of \$2,455,610, together with \$146,503 of interest accrued and unpaid thereon to January 1, 1939, subject to the reduction of said amounts by the application, prior to the date of issue of the new securities under the plan, of any proceeds from the distributive shares of the company or its subsidiaries under the marshalling and distributing plan, 1931, approximately \$154,111 of income-mortgage 4½ percent bonds, series A; \$241,681 of 5-percent preferred stock, series A; and 35,425 shares of common stock, being common stock taken at the price of \$62 per share. The Railroad Credit Corporation's equity in the collateral securing the claim of the Reconstruction Finance Corporation is found to be without value.” (TR-10962, p. 72).

Subdivision R of the plan provides, in part:

“* * * All collateral pledged by the debtor as security for notes to the Reconstruction Finance Corporation, the Railroad Credit Corporation, and the A. C. James Company shall be reduced to possession by the respective pledgees thereof, and shall be surrendered by them to the reorganized company and canceled, except that the Railroad Credit Corporation shall not release or surrender any right or interest in the distributive shares of the debtor or its subsidiaries under the marshaling and distributing plan, 1931, but any proceeds from such distributive shares after the effective date of the plan shall become the property of and be retained by the Railroad Credit Corporation, but to the extent to which received prior to the issue of the new securities under the plan shall be applied in reduction of the claim of the Railroad Credit Corporation in respect of which such new securities are to be issued at the rates provided in subdivision P. * * *” (TR-10962, pp. 73-74).

The Commission's original Report of October 10, 1938, provided that all collateral pledged by the debtor to Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Company should be surrendered to the debtor and:

“* * * The Railroad Credit Corporation also should release and surrender to the reorganized company its rights and interests in the debtor's distributive shares under the marshaling and distributing plan, 1931, from and after the effective date of the plan, and any proceeds from such shares applied by the Railroad Credit Corporation to the payment of principal and/or interest of and upon the obligations of the debtor after the effective date of the plan, unless such application shall have been made by authority of the court of competent jurisdiction, shall be turned over to the reorganized company.” (TR-9714, p. 280).

The Commission's original Order dated October 10, 1938, contained a corresponding provision, requiring The Railroad Credit Corporation to surrender to the reorganized company all its right and interest in the debtor's distributive shares under the Marshalling and Distributing Plan of 1931 (TR-9714, pp. 297-8).

Upon petitions for modification of the Commission's original Report and Order, the Credit Corporation objected to the provision requiring it to release and surrender the distributive shares of the debtor and its subsidiaries under the Marshalling and Distributing Plan, and, for reasons which are not at all clear, the Commission, in its Report of June 21, 1939, modified this provision and stated:

“Under the bondholders' committee's modified plan, existing mortgages on the debtor's properties would be released and canceled * * *. All collateral pledged by others than the debtor * * * would be surrendered to the pledgors thereof, and all collateral pledged by the debtor as security for such notes would be reduced to possession by the respective pledgees thereof, and would then be by them surrendered to the reorganized company and canceled, except that the Credit Corporation would not release or surrender any right or interest in the distributive shares of the debtor or its subsidiaries under the marshaling and distributing plan, 1931, but any proceeds from such distributive shares after the effective date of the plan, would become the property of and be retained by the Credit Corporation, but to the extent to which received prior to the issue of the new securities under the plan would be applied in reduction of the claim of the Credit Corporation.” (TR-9714, p. 344).

The Commission then approved these proposals (except that which provided for surrender of collateral pledged by others than the debtor) and adopted the provisions of paragraph 4 of subdivision P of the plan, quoted above, and the provisions of subdivision R which are quoted above.

No question was raised by The Railroad Credit Corporation or any other party before the District Court as to the provisions of the plan of reorganization which relate to the retention by The Railroad Credit Corporation of the distributive shares of the debtor and its subsidiaries under the Marshalling and Distributing Plan of 1931. Nor, indeed, was it to be expected that any such question would be raised by the Credit Corporation since it had been accorded by the Commission a privilege not extended to any other secured creditor of the debtor and was permitted to retain collateral pledged by the debtor (cash or its equivalent), notwithstanding the order of the District Court dated August 2, 1935, enjoining the sale, disposition, or conversion of such collateral. No other secured creditor was permitted, under the terms of the plan, to retain any collateral pledged by the debtor.

No question having been raised in the District Court as to the retention by the Credit Corporation of the marshalling and distributing payments, no question was presented to the Supreme Court and no issue was made of this matter before that Court.

Only when the time approached for the consummation of the plan, and after the plan had been accepted by The Railroad Credit Corporation and all other classes, did the Credit Corporation raise any question as to the meaning of the provisions of the plan relative to the retention by the Credit Corporation of the distributive shares of the debtor and its subsidiaries under the Marshalling and Distributing Plan of 1931. Upon the petition of the Reorganization Committee, as stated above, the District Court proceeded to construe these provisions of the plan.

The Court was authorized to make a “*final and conclusive*” construction of any provision of the plan of reorganization by subdivision V, which provides:

“V. The construction of the plan by the court shall be final and conclusive. The court may cure any defect, supply any omission, or reconcile any inconsistency in such manner or to such extent as may be necessary or expedient in order to carry out the plan effectively.” (TR-10962, p. 69).

The provisions of paragraph 4 of subdivision P of the plan, quoted above, which relate to the application of the proceeds of the distributive shares of the debtor and its subsidiaries under the Marshalling and Distributing Plan of 1931, require a reduction in the claim of The Railroad Credit Corporation by the amount of proceeds of such distributive shares applied by the Credit Corporation after December 31, 1938, and prior to the issue of the new securities under the plan. The provisions of subdivision R, quoted above, expressly require a reduction in the “claim of The Railroad Credit Corporation in respect of which such new securities are to be issued at the rates provided in subdivision P.” The extracts from the Commission’s reports clearly provide for a reduction in the Credit Corporation’s claim by the amount of such proceeds.

The Commission dealt with the claim of The Railroad Credit Corporation as a unit. The reports contain no reference to any unsecured claim of the Credit Corporation and no finding that the Credit Corporation’s claim was not fully secured by the debtor’s collateral held by it. In its original report, the Commission declared that the common stock available for distribution to Reconstruction Finance Corporation, The Railroad Credit Corporation, and A. C. James Company was inadequate in value to satisfy in full the aggregate of their secured claims (TR-9714, p. 271), but made no determination as to the amount of such inadequacy. However, the allocation of common stock to The Railroad Credit Corporation at \$62 a share makes it clear that for the purposes of the plan the common stock allocated to the Credit Corporation had this valuation, so that the

Credit Corporation's claim was fully secured and fully paid. It was the claim of A. C. James Company which was not fully secured and not fully paid. The District Court so held (TR-10962, pp. 105, 107); and the Supreme Court referred to this fact (318 U. S. at 488).

2. Appellant's Contentions

Counsel for The Railroad Credit Corporation claim that the Interstate Commerce Commission determined the value of the debtor's general and refunding bonds held in pledge by the Credit Corporation at \$1,437,346 and allocated to the Credit Corporation new securities only in respect of that part of its claim which was secured by such bonds, and that the distributive shares of the debtor and its subsidiaries under the Marshalling and Distributing Plan in the amount of \$26,091.72 should be considered as applied in reduction of the balance of the Credit Corporation's claim, leaving \$1,463,437 of the claim unsecured except by the third party collateral held by the Credit Corporation (Brief, pp. 17, 35).

It is even asserted (Brief, pp. 36 ff.) that the Credit Corporation was entitled to be treated as a senior creditor with full priority rights (though subdivision P of the plan of reorganization finally approved by the Supreme Court and accepted by the Credit Corporation itself treats the Credit Corporation as a junior creditor), and the special privilege of realizing on debtor's collateral in defiance of the District Court's restraining order of August 2, 1935 (TR-9714, pp. 10-20, par. 4). From this line of reasoning counsel would draw the conclusion that the Credit Corporation is entitled to retain the distributive shares of the debtor and its subsidiaries under the Marshalling and Distributing Plan of 1931, without a corresponding reduction in the securities allocated to it under the plan of reorganization.

This argument is not supported by the plan itself or by findings of the Commission and is wholly unsound.

3. Findings and Capitalization Approved by the Commission

The Commission made no finding either as to the value of the general and refunding bonds or as to the amount by which the aggregate claims of the secured creditors were not fully secured, and it is impossible to spell out from the Commission's reports any finding or suggestion that the Credit Corporation's claim was not refunded in full by the securities allocated to it. The Commission did find the value of certain assets pledged under the general and refunding mortgage upon which that mortgage admittedly constituted a first lien at approximately \$1,850,000; and on this basis approved an increase of \$732,010 principal amount of income mortgage bonds and \$1,147,955 par value of preferred stock to be issued in the reorganization (TR-9714, pp. 314-316). These additional securities were to be issued to the junior creditors, Reconstruction Finance Corporation, The Railroad Credit Corporation, and A. C. James Company. The major part of them were in fact allocated to Reconstruction Finance Corporation (subdivision P of the plan, TR-9714, p. 391). But the Commission neither discussed nor made any finding as to the value of the general and refunding mortgage's second lien on assets which were subject to the prior lien of the first mortgage, nor as to assets of the debtor not subject to either mortgage.

The capitalization of the reorganized Company approved and authorized by the Commission was in fact based on the Commission's estimate of probable earnings and not on property values (TR-9714, pp. 309-10). The Supreme Court, however, spelled out a determination of the value of the debtor's entire system from the "total face and assumed value of the securities authorized by the plan" (318 U. S. at 456, 487). The value so determined was \$84,000,000 plus. If we deduct from this total value the aggregate of the outstanding trustees' certificates, equipment obligations, and first mortgage bonds, principal and interest (\$75,000,000 plus), the remainder of \$9,000,000 should ap-

proximate the value of the assets subject to the lien of the general and refunding bonds and such assets as were not subject to any lien. This figure does not support the Credit Corporation's contention as to the value of the general and refunding bonds or as to the value of the security underlying the Credit Corporation's claim.

True, the Commission did find that the Credit Corporation's equity in the collateral securing the claim of Reconstruction Finance Corporation was without value (TR-9714, pp. 316, 392), a finding which may have been factually erroneous. This finding was an issue in the reorganization proceeding and was in fact attacked by the Credit Corporation before the Commission (TR-9714, p. 675), before the District Court (TR-955), and before this Court in No. 9714 (TR-1644-8).

Whether or not factually erroneous, the conclusion of the Commission that the Credit Corporation's equity in the collateral securing the claim of Reconstruction Finance Corporation was without value is now *res adjudicata* and not open to question upon this appeal.

Lacking a definite finding as to the dollar value of the general and refunding bonds and as to the amount by which the aggregate claims of the three secured creditors were not to be satisfied in full, the Commission could not have allocated definite amounts of new securities in payment of part only of the Credit Corporation's claim, but the Commission did not leave this conclusion to inference. The contention that new securities were allocated to the Credit Corporation in payment of only \$1,437,346 of its claim is disproved by the express language of the plan. Paragraph 4 of subdivision P of the plan, quoted above, allocates new securities to the Credit Corporation "in respect of its claim in the principal amount of \$2,455,610, together with \$146,503 of interest accrued and unpaid thereon to January 1, 1939" (subject to reduction by the application of marshaling and distributing payments).

The allocation of securities to Reconstruction Finance Corporation in full payment of its claim was made in identical terms (TR-9714, pp. 391, 392).

The formula by which counsel for the Credit Corporation determines the extent by which the Credit Corporation's claim was secured by general and refunding bonds held in pledge by it ignores completely the fact that the principal claim of Reconstruction Finance Corporation was in fact paid through the issue of new income mortgage bonds and preferred stock in the same proportions in which first mortgage bonds were refunded; and the accrued unpaid interest on the Finance Corporation's claim was paid in common stock at \$57 a share, the same rate at which the common stock was issued to first mortgage bondholders.

4. The Claims of Senior Creditors Were Refunded in Full

The fallacious character of the argument on behalf of the Credit Corporation is conclusively demonstrated by reference to the amounts and values of the securities allocated to the first mortgage bondholders and to Reconstruction Finance Corporation under the plan. Paragraph 2 of subdivision P provides:

"2. Holders of existing first-mortgage bonds shall receive for each \$1,000, principal amount thereof, together with \$266.66 $\frac{2}{3}$ of interest accrued and unpaid thereon to January 1, 1939, approximately \$400 of income-mortgage 4 $\frac{1}{2}$ -percent bonds, series A (being 40 percent of the principal amount of said existing bonds); \$600 of 5-percent preferred stock, series A (being 60 percent of the principal amount of said bonds); and 4.67 shares of common stock (being common stock taken at the price of \$57 a share for 100 percent of said accrued and unpaid interest)." (TR-9714, pp. 390, 391, par. 2)

Under the absolute priority doctrine of the *Boyd* case (R. C. C. Brief, p. 39; *Ecker v. Western Pacific R. Corp.*, 318 U. S. 483-8, 63 Sup. Ct. 692) the securities allocated to

first mortgage bondholders necessarily provided payment in full for the principal and interest of such bonds plus sufficient additional value to provide for compensation for their lost priority and for reduced interest and postponed maturity date on the new bonds. Upon no other basis could the Supreme Court have approved the plan. Likewise the securities allocated to Reconstruction Finance Corporation must necessarily have paid its claim in full.

The junior creditors, A. C. James Company and The Railroad Credit Corporation, were not entitled to receive one dollar of new securities (other than their proportionate share of the new income mortgage bonds and preferred stock issued in respect of the assets on which the general and refunding mortgage constituted a prior lien) until the first mortgage bonds were paid in full with additional compensation for loss of priority rights. Nor could new securities be allocated to A. C. James Company and The Railroad Credit Corporation at lower values or in amounts which were proportionately greater.

5. The Claim of The Railroad Credit Corporation Was Refunded in Full under the Plan

The Credit Corporation received in respect of its claim with interest (total \$2,590,924) the following:

Income Mortgage Bonds	\$ 154,111	\
Preferred Stock	241,681	
Common Stock at a Value of \$62 a		
Share	2,196,350	
<hr/>		
Total	\$2,592,142	

As a result of the necessity of compensating first mortgage bondholders for loss of their priority rights (*Ecker v. Western Pacific R. Corp.*, 318 U. S. at 484, 488, 63 Sup. Ct. 692; *Group of Investors v. Milwaukee R. Co.*, 318 U. S. 523 at 563, 569-70, 63 Sup. Ct. 727), the rule of absolute priority

required the issuance of common stock to them at a somewhat lower price than it was issued to the Credit Corporation (that is, at \$57 a share, as was expressly provided in paragraph 2 of subdivision P of the plan). Hence the plan provided for refunding in full the claim of the Credit Corporation by the issue to it of the securities listed above.

Thus it was, of course, not possible under the plan and the doctrine of absolute priority as announced and reaffirmed by the Supreme Court, to allocate to the Credit Corporation \$154,111 of income bonds, \$241,681 of preferred stock, and 35,425 shares of common stock in payment of only \$1,437,346 of its claim. To do so would result in the issue of common stock to the Credit Corporation at a value of \$29.40 per share after issuing to it the income mortgage bonds and preferred stock. The Commission could provide for the issue of common stock to the Credit Corporation at a higher rate than it was issued to first mortgage bondholders (at \$62 a share as was done) but not at the rate of \$29 a share as contended by counsel for the Credit Corporation.

The argument as to the value of general mortgage bonds securing the Credit Corporation's claim and all conclusions drawn therefrom fail completely, *first*, because they are inconsistent with the findings and capitalization approved by the Commission and with the provisions of the plan as a whole, and *secondly*, because they would necessarily indicate a violation of the absolute priority doctrine upon which the Supreme Court has placed so much emphasis.

POINT II

The Credit Corporation's rights in debtor's collateral, under its contract of pledge, were subject to modification in the reorganization proceeding.

The brief on behalf of the Credit Corporation, appellant, pages 36-45, discusses at some length the contractual rights of the Credit Corporation under the Marshalling and Dis-

tributing Plan of 1931, and under the pledge agreement between it and the Railroad Company given in connection with the collateral notes of the Railroad Company upon which the claim of the Credit Corporation is based. Whatever rights the Credit Corporation may have had prior to the commencement of the reorganization proceedings in August, 1935, it is obvious that its contractual rights were curtailed by the reorganization proceedings and by the Court's order enjoining the sale or other disposition of collateral held by the Credit Corporation. Thereafter the Credit Corporation was entitled to receive only such new securities as should be allocated to it by the plan of reorganization as finally confirmed, and, upon the consummation of the plan, would be required to surrender the collateral pledged by the debtor.

The first mortgage bondholders, Reconstruction Finance Corporation and A. C. James Co. were required upon consummation of the plan to surrender all debtor collateral held by them as security.

The power of the Commission and the District Court to deal in this manner with debtor collateral held by secured creditors was sustained by the decisions of the Supreme Court in the *Western Pacific* case and the *Milwaukee* case. It was established prior to these decisions in *Continental Illinois National Bank v. Chicago, Rock Island & Pacific Ry. Co.*, 294 U. S. 648, 55 Sup. Ct. 595.

A creditor in a reorganization proceeding holding collateral pledged by the debtor may be enjoined from disposing of such collateral and required to surrender it upon consummation of the reorganization. If he is permitted to retain and apply such collateral, his claim and the securities allocated to it must be reduced pro rata.

POINT III

The construction by the District Court of the provisions of the Plan relating to the Marshalling and Distributing payments is final and conclusive.

Subdivision V of the plan provides:

“V. The construction of the plan by the court shall be final and conclusive. The court may cure any defect, supply any omission, or reconcile any inconsistency in such manner or to such extent as may be necessary or expedient in order to carry out the plan effectively.” (TR-10962, p. 69).

If there is any doubt as to the meaning of paragraph 4 of subdivision P and subdivision R of the plan, in so far as they deal with the distributive shares of the debtor and its subsidiaries under the Marshalling and Distributing Plan of 1931, it is beyond question that the Commission might have spelled out that meaning in express words or might have indicated its construction of the language used by it in the plan, and the meaning and construction adopted by the Commission would have been binding on The Railroad Credit Corporation and all parties after final confirmation of the plan. The Commission anticipated that controversies might arise as to the proper construction of the plan and its provisions. In consequence, subdivision V was inserted in the plan by the Commission for the express purpose of authorizing the District Court to make a final and conclusive construction of any questioned provision of the plan, to the extent that the Commission itself might have made a final and conclusive determination as to the proper construction. It should be noted that the construction of the plan by the Court is to be “*final and conclusive.*” By accepting the plan the Credit Corporation in effect stipulated that no appeal would be taken from the District Court’s construction order (*United States Consol. Seeded*

Raisin Co. v. Chadock & Co., 173 Fed. 577, 9th Circ.; *In re Patterson-MacDonald Shipbuilding Co.*, 292 Fed. 700, 9th Circ., cert. denied 266 U. S. 638; *Hoste v. Dalton*, 137 Mich. 522, 100 N. W. 750).

It follows that by the provisions of the plan itself, as finally approved by the District Court and the Supreme Court of the United States and confirmed by the District Court after a favorable vote of acceptance by all classes of secured creditors, including the Credit Corporation, the construction of the plan by the Court is to be final and conclusive. In view of these considerations, this Court should not overturn the determination of the District Court as to the proper construction of the provisions of paragraph 4 of subdivision P and subdivision R, relative to the effect of the retention by the Credit Corporation of the distributive shares of the debtor and its subsidiaries under the Marshalling and Distributing Plan of 1931, particularly where the construction adopted by the District Court is supported by the express language of the plan itself.

Conclusion

Paragraph (3) of the District Court's construction order of September 14, 1944 and the findings in support thereof should be affirmed or, in the alternative, the appeal should be dismissed.

Respectfully submitted,

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